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Online Reputation and the Regulation of Information Asymmetries in the Platform Economy

Sofia Ranchordás*

Abstract

In recent years, online rating and reputational mechanisms have become increasingly important in the regulation of behavior in the platform economy. Consumers tend to rely on online reviews to distinguish between service providers both in the business-to-consumer and the peer-to-peer economy. The European Commission and the Federal Trade Commission, as well as a strand of legal scholarship, have praised these online mechanisms for generating valuable information while reducing market failures and consumer risks. However, this position has overlooked evidence suggesting that the additional data provided by online reputation might not be able to address information asymmetries and manage risks due to the multiple shortcomings of existing online reputational mechanisms. In this article, I discuss the regulatory potential of online reputational feedback and offer a nuanced reflection on the traditional assumption that the availability of more information in the market reduces the need for public regulation. I suggest a co-regulatory framework for the regulation of online reputation that could help promote the transparency and trustworthiness of these informal enforcement mechanisms.

I. Introduction

Nowadays, after a visit to a hotel or restaurant, the most effective way of giving a compliment on a service might be to write a positive review on one of the countless booking and review websites such as Booking.com, Tripadvisor, or Yelp.¹ The ubiquity of these reputational systems has been discussed in the past decade in the media and satirized in popular shows. In the American sitcom *Community*, “MeowMeowBeenz” is presented as a groundbreaking monitoring device that would allow students to rate both students and teachers and create a system where community members would be segregated on the grounds of their ratings. More recently, the Netflix show *Black Mirror*

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¹ Catheryn Khoo-Lattimore & Erdogan H. Ekiz, Power and Praise: Exploring Online Compliments on Luxury Hotels, 14 *Tourism & Hospitality Res.* 152 (2014).

took its viewers to a futuristic world where individuals are dominated by the fear of receiving low ratings. Such systems may seem like a frivolous matter pertaining primarily to the world of popular culture and having little legal relevance.² However, a closer look at the impact of these reputational systems demonstrates that a sterile world of constant online monitoring and peer-review has been regulating several segments of our society for the past ten years with a level of granularity and control that the strictest regulators would envy.³

Reputation and word-of-mouth have, for centuries, been regarded as alternatives to formal enforcement mechanisms, as they generate trust and provide a great deal of information to consumers. Relying on reputation is instinctive to humans and it is naturally perceived as a key instrument to promote cooperation.⁴ Indeed, the reliance on an individual's good name has historically preceded state interventions such as modern authorization schemes (e.g., licenses, permits), periodic inspections, product liability rules, and regulatory sanctions. In the diamond or cotton industries, merchant traders reliably fulfilled their contractual obligations without the threat of regulation and public courts,⁵ while investors decided whether a country would be likely to honor its debts based on the country's reputation.⁶ In the last half-century, there has been a revival of interest in the interdisciplinary study of reputation, particularly with the development of the sharing economy and the flowering of user-generated content on platforms like Yelp.⁷ One of the key questions that remains unanswered in the literature is whether online ratings and reviews can replace traditional regulation in the management of consumer risks.

² For an interdisciplinary analysis of reputation, see *The Reputation Society* (Hassan Masum & Mark Tovey eds., 2011).

³ See Clayton P. Gillette, *Reputation and Intermediaries in Electronic Commerce*, 62 *La. L. Rev.* 1165 (2002); Juan Jose Ganuza & Fernando Gomez, *Product Liability Versus Reputation*, 32 *J.L., Econ. & Org.* 213 (2013) (discussing the relationship between market reputation and product liability regulations, the costs of market reputation, and arguing that the level of legal liability should not be reduced or eliminated when market reputation is available); Cassandra Burke Robertson, *Online Reputation Management in Attorney Regulation*, 29 *Geo. J. Legal Ethics* 97 (2016) (discussing the regulatory and psychological dynamics from online reviews in attorney regulation).

⁴ John Whitfield, *The Biology of Reputation*, in *The Reputation Society*, supra note 2, at 39, 40.

⁵ Barak Richman, *How Community Institutions Create Economic Advantage: Jewish Diamond Merchants in New York*, 31 *Law & Soc. Inquiry* 383 (2006); Lisa Bernstein, *Opting Out of the Legal System: Extralegal Contractual Relations in the Diamond Industry*, 21 *J. Legal Stud.* 115 (1992); Lisa Bernstein, *Private Commercial Law in the Cotton Industry: Creating Cooperation Through Rules, Norms, and Institutions*, 99 *Mich. L. Rev.* 1724 (2001). But see Avner Greif, *Cultural Beliefs and the Organization of Society: A Historical and Theoretical Reflection on Collectivist and Individualist Societies*, 102 *J. Pol. Econ.* 912 (1994) (discussing the role of culture in contractual relationships and distinguishing between the Maghribi merchants' collectivist cultural beliefs that explained their reliance on reputation and information networks and the individualism of the Genoese traders, who preferred formal contractual enforcement mechanisms).

⁶ Michael Tomz, *Reputation and International Cooperation* (2007).

⁷ See, e.g., Werner Raub & Jeroen Weesie, *Reputation and Efficiency in Social Interactions: an Example of Network Effects*, 96 *Am. J. Soc.* 626 (1990); *The Reputation Society*, supra note 2; Grahame R. Dowling, *Winning the Reputation Game: Creating Stakeholder Value and Competitive Advantage* (2016); Lawrence McNamara, *Reputation and Defamation* (2007); Lucio Picci, *Reputation-Based Governance* (2011).

Regulators in Europe and the US as well as a strand of legal scholarship have suggested that online reputational mechanisms along with the self-regulatory practices implemented by digital platforms (e.g., background checks) are capable of addressing a number of market failures.⁸ The Federal Trade Commission (through its Economic Liberty Task Force) and the European Commission have praised the ability of reputational mechanisms to reduce information asymmetries in the peer-to-peer (“P2P”) economy.⁹

This position, however, overlooks the shortcomings of online reputational feedback, does not elaborate on the interaction between reputation and traditional regulation, and assumes that the existence of abundant information in the market automatically alleviates the information asymmetries that typically justify state intervention. But more information does not always mean more knowledge, particularly when there is still little transparency on how ratings and reviews are processed.¹⁰ Although rating and reputational mechanisms have an important regulatory potential, an uncritical reliance on these instruments can be particularly worrisome in the P2P economy, as user-generated content might be the only instrument that consumers have at their disposal to obtain information about the quality and safety of a product.

In this article, I discuss the extent to which online reputation is able to address informational market failures that typically justify the regulation of a number of services (e.g., the hospitality sector). I question whether these informal mechanisms would be suitable to complement or replace some—but not all—functions of traditional licensure.¹¹ Considering the shortcomings of reputational mechanisms and the accountability deficit that characterizes this type of informal enforcement, I suggest a model of co-regulation that could help promote the transparency of reputational systems. This article draws on the abundant legal, economic, and business literature on reputation, online word-of-

⁸ See Benjamin Klein & Keith B. Leffler, *The Role of Market Forces in Assuring Contractual Performance*, 89 *J. Pol. Econ.* 615 (1981); Chrysanthos Dellarocas, *The Digitalization of Word-of-Mouth: Promises and Challenges of Online Feedback Mechanisms*, 49 *Mgmt. Sci.* 1407 (2003); Adam Thierer et al., *How the Internet, the Sharing Economy, and Reputational Feedback Mechanisms Solve the “Lemons Problem,”* 70 *U. Miami L. Rev.* 830 (2016); Molly Cohen & Arun Sundararajan, *Self-Regulation and Innovation in the Peer-to-Peer Sharing Economy*, 82 *U. Chi. L. Rev. Dial.* 116 (2015).

⁹ Communication from the Commission to the European Parliament, The Council, the European Economic and Social Committee and the Committee of the Regions, *A European Agenda for the Collaborative Economy*, COM (2016), 356 final (June 2, 2016) (<https://ec.europa.eu/transparency/regdoc/rep/1/2016/EN/1-2016-356-EN-F1-1.PDF>) [hereinafter *European Agenda*]; Federal Trade Commission, *The “Sharing” Economy: Issues Facing Platforms, Participants & Regulators*, An FTC Staff Report (2016) (https://www.ftc.gov/system/files/documents/reports/sharing-economy-issues-facing-platforms-participants-regulators-federal-trade-commission-staff/p151200_ftc_staff_report_on_the_sharing_economy.pdf).

¹⁰ See Frank Pasquale, *Reforming the Law of Reputation*, 47 *Loyola U. Chi. L.J.* 515 (2015); Danielle Citron & Frank Pasquale, *The Scored Society: Due Process for Automated Predictions*, 89 *Wash. L. Rev.* 1 (2014).

¹¹ Sandeep Vaheesan & Frank Pasquale, *The Politics of Professionalism: Reappraising Occupational Licensure and Competition Policy*, *Ann. Rev. L. & Soc. Sci.* (forthcoming 2018) (https://papers.ssrn.com/sol3/papers.cfm?abstract_id=2881732).

mouth (“WoM”), and the sharing economy.¹² This article approaches the topic from the perspective of the broader transition from formal, public, expert-based regulation to a peer-to-peer regulatory state characterized by the growing intervention of private actors without particular expertise. Consumer-generated content is, in some cases, preferred to expert opinion because it is perceived as more independent and unbiased.¹³ This perception might not always be accurate. This article offers a nuanced reflection on the traditional assumption that the disclosure of more information can reduce information asymmetries and diminish the need for state intervention. In other words, more information about reputation does not necessarily demand “less regulation.”¹⁴

This article is organized as follows: Part I explains how online ratings and reputational mechanisms operate in the P2P economy and why they have become an important source of consumer information; Part II discusses the shortcomings of online reputational feedback; Part III discusses the shift from traditional command-and-control regulation to informal and peer-to-peer reputational schemes; and Part IV suggests a co-regulatory framework that could help the collaboration between private reputational systems and public authorization and enforcement mechanisms.

II. Online Rating and Reputational Systems

The development of the information society has empowered consumers, who now have the ability to access more information, compare services, and hire a large variety of on-demand providers for occasional services.¹⁵ In a globalized world, it has become increasingly challenging to obtain reliable information about these services. Ebay, Airbnb, EatWith, and many other P2P platforms rely on online ratings and reviews to attract new customers and help consumers distinguish between good and bad service providers. After each transaction, consumers are asked to write a review about the service they have experienced. In some cases, parties review each other’s performance and this reputational information will be publicly available for both current and prospective users of a specific platform.

The level of detail and usefulness of online reviews varies greatly, but it is now

¹² See, e.g., Christoph Busch, *Crowdsourcing Consumer Confidence: How to Regulate Online Rating and Review Systems in the Collaborative Economy*, in *European Contract Law and the Digital Single Market: The Implications of the Digital Revolution* 221 (Alberto de Franceschi ed., 2016); Christoph Busch et al., *Discussion Draft of a Directive on Online Intermediary Platforms*, 6 J. Eur. Consumer & Market L. 164 (2016).

¹³ Ann Marie Marciarille, “How’s My Doctoring?” Patient Feedback’s Role in Assessing Physician Quality, 14 DePaul J. Health Care L. 361, 371 (2012).

¹⁴ Lior Jacob Strahilevitz, *Less Regulation, More Reputation*, in *The Reputation Society*, supra note 2, at 63, 71 (suggesting a complementary role for reputation tracking); see also Lior Jacob Strahilevitz, *Reputation Nation: Law in an Era of Ubiquitous Personal Information*, 102 Nw. U. L. Rev. 1667 (2008).

¹⁵ Lauren I. Labrecque et al., *Consumer Power: Evolution in the Digital Age*, 27 J. Interactive Marketing 257 (2013). Consumer empowerment by information does not mean the consumer is always sovereign and is not limited in its choices; for a thorough analysis of these objections, see Adrian Kuenzler, *Restoring Consumer Sovereignty: How Markets Manipulate Us and What Law Can Do About It* (2017).

well established that online reputation facilitates not only P2P but also business-to-consumer (“B2C”) transactions.¹⁶ Ratings and reviews provide first-hand information about a user or product, rank service providers, and offer an (allegedly) independent judgment. This part of the article explains why so many actors—including regulators—place this amount of trust in online reputational mechanisms.¹⁷

A. Reputation: Information and Trust

Like our great-grandparents, we still rely on the oldest form of advertisement: word-of-mouth (“WoM”). WoM started being studied in the context of corporations in the 1960s by Johan Arndt, who defined it as “oral, person-to-person communication between a perceived non-commercial communicator and a receiver concerning a brand, a product, or a service offered for sale.”¹⁸ Since then, a vast amount of literature in the fields of marketing, business, socio-psychology, economics, and tourism management has documented the effect of WoM on the behavior of both consumers and corporations.¹⁹

1. Online Reputation as a Source of Information

Reputational mechanisms have been used throughout history to facilitate exchanges between strangers and to overcome linguistic and cultural barriers.²⁰ The information used to build a good or bad reputation constitutes an effective mechanism to change or improve the provider’s behavior, especially under uncertain conditions and asymmetric information.²¹ Nowadays, we observe that the information generated by online reviews is particularly relevant in the context of so-called “experience goods,” whose qualities will be known only after purchase and use.²²

Reputational models of informal enforcement can be divided into three categories: (i) reputation for ability; (ii) reputation for integrity; and (iii) reputation for performance.²³

¹⁶ Zhiwei Liu & Sangwon Park, What Makes a Useful Online Review? Implication for Travel Product Websites, 47 *Tourist Mgmt.* 140 (2015).

¹⁷ See Kenneth H. Craik, *Reputation: A Network Interpretation* (2009).

¹⁸ Johan Arndt, Word of Mouth Advertising and Informal Communication, in *Risk Taking and Information Handling in Consumer Behavior* (Donald F. Cox ed., 1967); Johan Arndt, Role of Product-Related Conversations in the Diffusion of a New Product, 4 *J. Marketing Res.* 291 (1967).

¹⁹ Dellarocas, *supra* note 8; Steven Tadelis, The Market for Reputations as an Incentive Mechanism, 110 *J. Pol. Econ.* 854 (2002).

²⁰ Avner Greif, Reputation and Coalitions in Medieval Trade: Evidence on the Maghribi Trader, 49 *J. Econ. Hist.* 857 (1989).

²¹ Lisa Trigg, Using Online Reviews in Social Care, 48 *Soc. Pol’y & Admin.* 361 (2014).

²² For a distinction between “experience” and “search goods,” see Philip Nelson, Information and Consumer Behavior, 78 *J. Pol. Econ.* 311 (1970); Philip Nelson, Advertising as Information, 82 *J. Pol. Econ.* 729 (1974).

²³ W. Bentley MacLeod, Reputations, Relationships and the Enforcement of Incomplete Contracts, CESifo Working Paper Series No. 1730; IZA Discussion Paper No. 1978 (May 2006) (<https://ssrn.com/abstract=885347>).

These different types of reputation may be present more in some sectors than in others (e.g., payment platforms will invest in their reputation for integrity) and they may also be cumulative. In the P2P home-sharing sectors, users providing services try to build a good reputation for friendliness, hospitality, and comfortable accommodation offerings. In the services sectors (e.g., car sharing), platforms ask users to rate service providers on their performance as well as on the safety of the vehicle.

An empirical study conducted by Pew Research in the United States has shown that an overwhelming majority of consumers (82%) read online reviews in order to decide which hotel, restaurant or electronic product to choose.²⁴ Online reviews are consulted on a regular basis as they are easily accessible, brief, and offer immediate information.²⁵ Reputational feedback mechanisms reduce search costs and help consumers navigate the vast amount of information published on digital platforms. A clear presentation of ratings and reviews decreases search costs, as consumers can choose to read only positive or negative comments or to view only the services that have been assessed positively. However, the abundance of online reviews has also meant that consumers bear additional cognitive costs as information becomes more difficult to process.²⁶ As George Stigler famously explained, consumers will only seek information until the point that search costs equal the value of the information; put another way, a greater number of reviews will not necessarily help consumers make a better decision.²⁷

A reputational feedback system is nevertheless effective only if consumers are willing to leave a rating or review after their purchase. In the abovementioned empirical study, Pew Research concluded that 71% of consumers aged 18-49 (and 49% of those age fifty and older) are indeed willing to leave a review after experiencing a service.²⁸ On many P2P platforms, users are required to review each other and can book the next transaction only after having reviewed their previous transaction. As the number of reviews grows on B2C and P2P platforms, reputational feedback has become one of the most important sources of information for consumers, providing them with an informative but low-threshold podium.²⁹

2. Online Reputation and Trust

Reputation is a social concept that lays the foundations for trust between strangers. Like other trust-based relationships, these systems ensure that users are willing

²⁴ Pew Research, Online Shopping & E-Commerce (Dec. 19, 2016) (<http://www.pewinternet.org/2016/12/19/online-reviews/>).

²⁵ Marciarille, *supra* note 13, at 371.

²⁶ Liu & Park, *supra* note 16.

²⁷ George J. Stigler, *The Economics of Information*, 69 J. Pol. Econ. 213 (1961).

²⁸ Pew Research, *supra* note 24.

²⁹ See Qiang Ye et al., *The Influence of User-Generated Content on Traveler Behavior: An Empirical Investigation on the Effects of E-Word-of-Mouth to Hotel Online Bookings*, 27 Comput. Hum. Behav. 634 (2011).

to expose themselves to certain vulnerabilities because they have positive expectations regarding the counterparty. Reputation is valuable when consumers and service providers expect to interact on multiple occasions with a set of agents (e.g., restaurateurs expect customers to return) and when there are sanctions in place for those who do not cooperate.³⁰ This repeated interaction means that if one of the parties does not live up to her reputation, the collaboration will come to an end or the cheating partner will be sanctioned (e.g., her account on the platform will be deactivated, her reputation will be damaged).³¹ Reputation thus promotes both trust and reciprocity in trade as parties have an interest in living up to expectations.³² In addition, businesses and individuals rely nowadays on online reviews to assess how well they are performing.³³

B. The Legal Relevance of Reputation

Given the importance and the fragile character of this asset, reputation is legally protected in different ways.³⁴ “Good name” and “reputation” have long been regarded in the literature, case law, and even some U.S. state constitutions³⁵ as “interest(s) justifying legal protection.”³⁶ Thus far, the legal relevance of reputation has been threefold. First, reputation has been protected against defamation through tort law.³⁷ Second, the sanction of naming and shaming engages the interest that corporations and individuals have in their reputations³⁸ The fear of reputational damage through this type of reputational sanction provides strong compliance incentives as the damage caused to reputation is often irreparable.³⁹ As the saying goes, “Trust arrives walking but it departs riding.” Third,

³⁰ Julia K. Lee, *Trust and Social Commerce*, 77 U. Pitt. L. Rev. 139 (2015).

³¹ Hans Caspar von der Crone & Johannes Vetsch, *Reputation and Regulation*, in *Reputation Capital: Building and Maintaining Trust in the 21st Century* 180 (Joachim Klewes & Robert Wreschniok eds., 2009); see also Paul Robert Milgrom & John Roberts, *Economics, Organization, and Management* (1992).

³² John Duffy et al., *Social Norms, Information and Trust Among Strangers: Theory and Evidence*, 52 *Econ. Theory* 669 (2013).

³³ Robert Sprague & Mary Ellen Wells, *Regulating Online Buzz Marketing: Untangling a Web of Deceit*, 47 *Am. Bus. L.J.* 415 (2010).

³⁴ Laura Heymann, *The Law of Reputation and the Interest of the Audience*, 52 *B.C. L. Rev.* 1341 (2001).

³⁵ Indiana Const., art. 1, § 12 (“[A]ll courts shall be open; and every person, for injury done to him in his person, property, or reputation, shall have remedy by due course of law.”)

³⁶ *Id.*

³⁷ See, e.g., Eric Descheemaeker, *Protecting Reputation: Defamation and Negligence*, 29 *Oxford J. Legal Stud.* 603 (2009); David A. Anderson, *Reputation, Compensation, and Proof*, 25 *Wm. & Mary L. Rev.* 747 (1984); Heymann, *supra* note 34; Robert C. Post, *The Social Foundations of Defamation Law: Reputation and the Constitution*, 74 *Cal. L. Rev.* 691 (1986).

³⁸ Naming and shaming sanctions tend to be more effective than financial penalties as they attack the most valuable asset of a firm: its good reputation. In the offline and online worlds, shaming sanctions are particularly relevant in communities where individuals interact on a regular basis and share common values. See David A. Skeel, Jr., *Shaming on Corporate Law*, 149 *U. Pa. L. Rev.* 1811.

³⁹ On the general impact of reputational sanctions, see Brent Fisse & John Braithwaite, *The Impact of Publicity on Corporate Offenders* (1983).

the legal relevance of reputation is also visible in its use as a complement to contractual arrangements and civil litigation.⁴⁰ This complementary character has been employed to reduce litigation costs, support executory contracts, and monitor product quality.⁴¹

III. The Shortcomings of Reputational Mechanisms

While ratings and reviews can be informative and can provide unique insights, reputational mechanisms operate in an obscure way. Platforms often organize comments strategically in order to down-rank negative comments and calculate ratings according to doubtful formulas.⁴² Therefore, the existing empirical studies on reputational mechanisms have revealed mixed results on the veracity and trustworthiness of these mechanisms.⁴³ In this Part, I explore the current shortcomings of online reputational mechanisms.

A. Content, Usefulness, and Objectivity of Review

When scrolling through major P2P platforms, we might quickly realize that the overwhelming majority of reviews are positive. This phenomenon has also been explored in the media, which found that some consumers leave “five-star reviews” due to feelings of guilt.⁴⁴ Consumers fear that a four-star-rating will not be sufficient for an Uber driver to keep her account so they give her a more generous score and fail to disclose some moderate flaws of the service. But, as underlined in the mentioned article, “When everything gets a five, nothing gets a five,” and the ability of ratings and reviews to influence behavior gets lost. One of the major shortcomings of online rating and reputational mechanisms resides in this biased and non-expert attitude of reviewers.

While the quality control exerted by online reviewers might be continuous and allow for a daily control of the performance of service providers, this evaluation will be done with varying standards of quality, hygiene, and value for money.⁴⁵

Research has shown that moderate, detailed, and well-written personal testimonials will be perceived by prospective consumers as more useful and credible.⁴⁶

⁴⁰ Barak D. Richman, *The Antitrust of Reputation Mechanisms: Institutional Economics and Concerted Refusals to Deal*, 95 Vand. L. Rev. 325 (2009).

⁴¹ See Ronald Gilson & Robert Mnookin, *Disputing Through Agents: Cooperation and Conflict Between Lawyers in Litigation*, 94 Colum. L. Rev. 509 (1994); Bernstein, *Opting Out*, supra note 5; Bernstein, *Private Commercial Law*, supra note 5; Juan Jose Ganuza, Fernando Gomes & Marta Robles, *Product Liability Versus Reputation*, J.L., Econ. & Org. 1 (2016); Klein & Leffler, supra note 8.

⁴² See Joseph M. Reagle, *Reading the Comments* (2015) (offering an extensive analysis of the diversity of online comments and exploring how some actors manipulate and monopolize reputational feedback).

⁴³ Frank Pasquale, *Reputation Regulation: Disclosure and the Challenge of Clandestinely Commensurating Computing*, in *The Offensive Internet: Privacy, Speech, and Reputation* 107 (Saul Levmore & Martha C. Nussbaum eds., 2010).

⁴⁴ Ethan Wolff-Mann, *Here’s Everything Wrong with Online Reviews and How to Fix It*, Time (July 22, 2016) (<http://time.com/money/page/online-reviews-trust-fix/>).

⁴⁵ Vasiliki Baka, *The Becoming of User-generated Reviews: Looking at the Past to Understand the Future of Managing Reputation in the Travel Sector*, 53 Tourism Mgmt. 148, 158 (2016).

However, the same study also underlines that those same online reviews will influence consumers differently, for they tend to identify themselves more with some types of content and style rather than with others.⁴⁷ What is said, how it is said, and who says it can influence the assessment of the credibility of reviews as well as their impact on prospective behavior in many ways.⁴⁸

To illustrate, in the case of Airbnb (and other sharing economy platforms), prospective guests make decisions on whether or not to trust the host partially based on her personal photos or social media profile.⁴⁹ Individuals generally perceive uncertainty in interpersonal relationships as an unpleasant element, and so the disclosure of one's identity helps build trust among participants in the digital economy.⁵⁰ This trust is, therefore, derived from subjective elements that are not explained by the reviewer's ability to assess a service accurately.

B. Fake Reviews and other Unfair Practices

Online rating and reputational mechanisms suffer from the same problem as any other type of user-generated content: reviews are unfiltered, directly produced by users, and are often connected to social media profiles.⁵¹ In this context, it is difficult to assess the veracity of the review and limit the spread of “opinion spam,” meaning fake reviews and deceptive messages.⁵² Designing a system that incentivizes honest reviews and penalizes deceptive comments remains challenging: low-threshold systems might be easily manipulated by providers but complex systems will face limited consumer participation. Contrary to some service providers or product sellers, platforms have a direct interest in guaranteeing a trustworthy environment and, therefore, have incentives to encourage consumers to give their honest opinions on services.⁵³

At the time of writing, at least two European regulators are devoting attention to the need to improve the transparency and trustworthiness of online rating and reputational mechanisms. The UK Competition & Market Authority (CMA) has been gathering information on online reviews and endorsements since 2015 and working with

⁴⁶ Blanca Hernandez-Ortega, Don't Believe Strangers: Online Consumer Reviews and the Role of Social Psychological Distance, 55 *Info. & Mgmt.* 31 (2018) (https://www.researchgate.net/publication/315898293_Don't_Believe_Strangers_Online_Consumer_Reviews_and_the_Role_of_Social_Psychological_Distance).

⁴⁷ *Id.*

⁴⁸ Liu & Park, *supra* note 16.

⁴⁹ Eyal Ert et al., Trust and Reputation in the Sharing Economy: The Role of Personal Photos in Airbnb, 55 *Tourism Mgmt.* 62 (2016).

⁵⁰ Hernandez-Ortega, *supra* note 46.

⁵¹ Marco Viviani & Gabriella Pasi, Quantifier Guided Aggregation for the Veracity Assessment of Online Reviews, 32 *Int'l J. Intelligent Sys.* 481 (2017).

⁵² *Id.*

⁵³ Lirong Chen et al., Who Should Pay for Online Reviews? Design of an Online User Feedback System, 23 *Electronic Com. Res. & Applications* 38 (2017).

platforms to address potentially misleading practices, such as the publication of fake reviews, omission of negative reviews, and paid reviews.⁵⁴ In 2016, the CMA took action against an online marketing company that posted fake reviews and breached the Consumer Protection from Unfair Trading Regulations 2008.

In May 2017, the Dutch Authority for Consumers and Markets released the outcomes of a consumer survey, concluding that more transparency in the publication and management of reviews is required.⁵⁵ The Dutch regulator established that consumers currently make use of online reviews to a substantial and increasing degree, particularly when choosing electronic products, hotels, and restaurants. However, consumers do not rely on online reviews only in the orientation phase but remain critical and aware that some reviews might have been deleted or that their content might not be trustworthy.⁵⁶

C. Transparency and Due Process Rights

At a time when the lives of users have become increasingly transparent and subject to extensive scrutiny and constant review, secrecy is still the norm for the digital platforms that rely upon rating and reputational mechanisms.⁵⁷ It is, for example, often unclear why users see some reviews first even though they do not reflect the most recent transactions. On the “Support Center” page of Yelp, the platform tries to provide more information to users on “how Yelp decides which reviews to feature in the search results,”⁵⁸ but their answer—“the review snippets that appear on search result pages are determined algorithmically like the search ranking themselves”—does not shed much light on the question. Although the use of algorithms appears to confer an objective character on the platform’s decision-making, these algorithms are informed by data that reflect certain preferences.⁵⁹

At the moment, there is little transparency surrounding information selection and few rules that can ensure reputational integrity in the platform economy. This obscurity affects not only the legitimacy of online reputational mechanisms but also the due process

⁵⁴ Competition Market & Competition Authority, Online Reviews and Endorsements (<https://www.gov.uk/cma-cases/online-reviews-and-endorsements>).

⁵⁵ Dutch Authority for Consumers & Market, Press Release: ACM Calls for Increased Transparency in Online Reviews (May 11, 2017) (<https://www.acm.nl/en/publications/publication/17222/ACM-calls-for-increased-transparency-in-online-reviews/>).

⁵⁶ See also Jason Q. Zhang et al., When Does Electronic Word-of-Mouth Matter? A Matter of Consumer Product Reviews, 63 J. Bus. Res. 1336 (2010) (evaluating the different impacts of reviews depending on the consumption goal).

⁵⁷ See David Brin, *The Transparent Society* (1999) (exposing the paradox between the growing exposure of individuals to privacy-invasive technologies and the secrecy of powerful corporate and governmental monopolies).

⁵⁸ Yelp, Yelp Support Center (https://www.yelp-support.com/article/How-does-Yelp-decide-which-reviews-to-feature-in-search-results?l=en_US).

⁵⁹ Rob Kitchin, Thinking Critically About and Researching Algorithms, 20 Info., Comm. & Soc. 14, 18 (2017).

right of individuals.⁶⁰ Despite the lack of expertise and accuracy, negative reviews—though scarce—have a disproportionate effect on consumer behavior and may have disastrous consequences for users.⁶¹ A low rating or a number of negative reviews can result in the deactivation of a service provider’s account without the right to contest the content of these ratings or reviews. Online reputational mechanisms add to the current problem of constant workplace surveillance and enhanced pressure to perform under permanent monitoring.⁶²

A right to respond to unfavorable ratings and reviews has been defended for a number of years in the literature, but there is evidence that service providers’ responses can often be counterproductive.⁶³ Individuals tend to perceive negative reviews as personal attacks and respond in a defensive and irrational manner.⁶⁴

D. Legitimacy and Accountability

Meaningful accountability for ratings and reviews is also lacking in the platform economy. Rating and reputational platforms tend to be exempt from any form of liability as long as they operate in “good faith” and remove material that they believe to be obscene or violent.⁶⁵ In Europe and in the United States digital platforms are typically not responsible for user-generated content as long as they only host that content.⁶⁶ This leaves us with an accountability deficit: in the platform economy, no one is held accountable for the information produced on these platforms and the deficient quality and safety assessment conducted by the reviewers. It is the users’ responsibility to be critical when choosing a P2P service but platforms have not been included in this equation. Thus far, there have been attempts to hold sites that provide ratings of attorneys and physicians more accountable for the content produced by users.⁶⁷

The literature and regulators are thus at a crossroads: on the one hand, online rating and reputational mechanisms have become important information sources that

⁶⁰ Pasquale, *supra* note 10; see also Woodrow Hartzog & Evan Sellinger, *Surveillance as Loss of Obscurity*, 72 Wash. & Lee L. Rev. 1343 (2015).

⁶¹ M.S. Balaji et al., *Determinants of Negative Word-of-Mouth Communication Using Social Networking Sites*, 53 Info. & Mgmt. 528 (2016).

⁶² See Ifeoma Ajunwa et al., *Limitless Worker Surveillance*, 105 Cal. L. Rev. 735 (2017) (offering an extensive analysis of the problem of ubiquitous workplace surveillance and the need to protect worker privacy).

⁶³ Frank Pasquale, *Rankings, Reductionism, and Responsibility*, 54 Clev. St. L. Rev. 117 (2006); Robertson, *supra* note 3.

⁶⁴ The literature has documented why individuals react irrationally to criticism. See Andrew M. Perlman, *A Behavioral Theory of Legal Ethics*, 90 Ind. L.J. 1639 (2015); Peter M. Gollwitzer & John A. Bargh, *The Psychology of Action: Linking Cognition and Motivation to Behavior* (1996).

⁶⁵ Gus Hurwitz, *Trust and Online Interaction*, 161 U. Pa. L. Rev. 1579 (2013).

⁶⁶ See James Grimmelman, *The Structure of Search Engine Law*, 90 Iowa L. Rev. 1, 36 (2007).

⁶⁷ *Browne v. Avvo*, 525 F. Supp. 2d 1249 (W.D. Wa. 2007); see Grimmelman, *supra* note 66.

influence both consumers and service providers while, on the other, these mechanisms remain subjective, biased, and unreliable. The following Part explores this paradox in the context of the shift from traditional regulation to P2P validation.

IV. Regulation: From Command-and-Control to Peer-to-Peer Regulation

The sharing economy has disrupted longstanding sets of national and local regulations, particularly in the sectors of private transportation, hospitality, and restauration, where actors are required to comply with both *ex ante* and *ex post* regulations (e.g., licenses, permits, occasional or regular inspections).⁶⁸ Sharing economy platforms question the need for these longstanding rules, arguing that their self-regulatory model promotes economic growth and flexibility that is highly appreciated by users.⁶⁹ In addition, these platforms have put pressure on regulators to be more transparent about the real goals of public intervention and its ability to address public interests.⁷⁰ Platforms and supporters of the sharing economy also argue that rating and reputational systems address potential concerns and reduce risks to the public.⁷¹ Not surprisingly, service providers operating in the traditional sectors, consumer organizations, scholars concerned with the negative externalities of platform capitalism, and multiple national regulators beg to differ.⁷²

Unlicensed sharing economy services have caused much uproar, both in the literature and in physical spaces, with numerous demonstrations carried out in large European and American cities. In European countries such as Belgium, Germany, and the Netherlands, courts and sectorial regulators have prohibited these services and even imposed criminal sanctions on unlicensed Uber drivers.⁷³ The value of online reputational mechanisms has been rarely considered in these decisions as a risk-management tool, despite the European Commission's favorable position toward online ratings and reviews.

In a 2016 Communication, "A European Agenda for the Collaborative Economy," the European Commission praised online reputational mechanisms for

⁶⁸ See Sofia Ranchordás, Does Sharing Mean Caring? Regulating Innovation in the Sharing Economy, 16 Minn. J.L. Sci. & Tech. 414 (2015); Stephen Miller, First Principles for Regulating the Sharing Economy, 53 Harv. J. Legis. 147 (2016).

⁶⁹ For an overview of the different narratives in this context, see Frank Pasquale, Two Narratives of Platform Capitalism, 35 Yale L. & Pol'y Rev. 309 (2016).

⁷⁰ Nestor Davidson & John J. Infranca, The Sharing Economy as an Urban Phenomenon, 34 Yale L. & Pol'y Rev. 216 (2016).

⁷¹ Thierier et al., *supra* note 8.

⁷² See, e.g., Brishen Rogers, The Social Costs of Uber, 82 U. Chi. L. Rev. Dial. 85 (2015); Miriam A. Cherry, A Taxonomy of Virtual Work, 45 Ga. L. Rev. 951 (2011); Trebor Scholz, Platform Cooperativism vs. the Sharing Economy, MEDIUM (Dec. 5, 2014) (<http://medium.com/@trebors/platform-cooperativism-vs-the-sharing-economy-2ea737f1b5ad>); Ours to Hack and to Own: The Rise of Platform Cooperativism, A New Vision for the Future of Work and a Fairer Internet (Trebor Scholz & Nathan Schneider eds., 2016); Tom Slee, What's Yours Is Mine: Against the Sharing Economy (2015).

⁷³ Caroline Cauffman & Jan Smits, The Sharing Economy and the Law, 23 Maastricht J. EU & Comp. L. 903 (2016).

“discourag[ing] harmful behavior by market participants [and] . . . in some cases reduc[ing] risks for consumers stemming from information asymmetries.”⁷⁴ The European Commission highlighted that these mechanisms could “reduce the need for certain elements of regulation, provided adequate trust can be placed in the quality of the reviews and ratings.”⁷⁵ The European Commission also advised national regulatory bodies to limit their regulatory interventions to the strict protection of the public interest in line with the existing Internal Market rules and the Services Directive. It further advised them to consider the specific features of collaborative economy business models as well as “the tools they may put in place to address public policy concerns, for instance in relation to access, quality or safety.”⁷⁶

The Federal Trade Commission (“FTC”) has, thus far, followed a similar approach in its 2016 report on the sharing economy, which underlined the importance of rating and reputational mechanisms for the reduction of information asymmetries and other risks in the sharing economy.⁷⁷ Both regulators appear to acknowledge the ability of online rating and reputational mechanisms to replace or complement traditional regulation in the P2P and B2C economies but do not explain whether they respond to the traditional criticism to command-and-control regulation. This Part offers a reflection on this subject by drawing upon the foundational literature on public and private-interest regulation.

A. Public vs. Private Interest Theories of Regulation

Regulation traditionally refers to top-down, deliberate attempts of the state to address market failures and protect the public interest.⁷⁸ Although this traditional idea of command-and-control standards and rules still reigns in practice, there is no generally accepted definition of regulation nor of its toolbox.⁷⁹ A broader definition of regulation would, therefore, encompass all forms of social control, whether intentional or not, stemming from either public or private organizations.⁸⁰ An oft-cited definition of regulation places the emphasis on the instrumental function of regulation, stating that regulation is “[t]he sustained and focused attempt to alter the behavior of others according to standards or goals with the intention of producing a more broadly identified outcome or outcomes, which may involve mechanisms of standard-setting, information-

⁷⁴ Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions, A European Agenda for the Collaborative Economy, COM (2016) 356 final.

⁷⁵ *Id.*

⁷⁶ *Id.*

⁷⁷ Federal Trade Commission, *supra* note 9.

⁷⁸ See Anthony Ogus, *Regulation: Legal, Form and Economic Theory* (2004).

⁷⁹ OECD, *OECD Report on Regulatory Reform: Synthesis* (1997) (<https://www.oecd.org/gov/regulatory-policy/2391768.pdf>).

⁸⁰ Bronwen Morgan & Karen Yeung, *An Introduction to Law and Regulation* 3-4 (2007).

gathering and behavior-modification.”⁸¹ In the platform economy, a great deal of social control is exerted by P2P monitoring. Ratings and reviews set standards of quality that allow consumers to distinguish between the different service providers.

At the moment, the platform economy is characterized by different regulatory situations: licensed hotels and restaurants that use booking platforms such as Booking.com, Expedia, or OpenTable are subject to an array of public regulations, such as licensing schemes, but also take into account online reputational mechanisms. In the P2P economy, there is limited or no public control of the services provided on digital platforms and users rely primarily on rating and reputational mechanisms to obtain information on a service’s quality and safety. The relatively low number of incidents, the longstanding objections to the obsolescence of traditional regulation, and the need to advance less burdensome rules support the suggestion that self-regulation and online reputation could potentially replace state intervention. Nevertheless, as this section explains, the shift from public to P2P regulation implicates a deeper analysis of the ability of reputational mechanisms to address market failures effectively.

Public interest theories of regulation justify regulatory intervention with the need to promote social welfare and address market failures, such as negative externalities like noise.⁸² In the hospitality sector, the information asymmetry between the service providers and consumers, along with the health and safety risks to which a consumer is exposed when eating or sleeping at a foreign establishment, justified the need for the extensive regulation of entry.⁸³ In all of these cases, regulation (e.g., operating licensure, certification) is justified by the existence of information asymmetries and the consequent inability of consumers to assess the performance of a service provider before engaging in a transaction.⁸⁴

In the European Union, the regulation of entry is subject to a number of limitations. While Member States may regulate access to certain professions, national requirements should be justified by the protection of the public interest. In addition, Member States are required to reduce or eliminate any disproportionate barriers to the freedom of circulation of services. National authorization schemes must be based on clear, unambiguous, transparent, and objective criteria to prevent the arbitrariness of

⁸¹ Julia Black, What Is Regulatory Innovation, in *Regulatory Innovation* 11 (Julia Black et al. eds., 2005). This definition also draws on the work of Christopher Hood et al., *The Government of Risk* (2001).

⁸² W. Kip Viscusi et al., *Economics of Regulation and Antitrust* 381 (2005); Johan den Hertog, Review of Economic Theories of Regulation, Discussion Paper no. 10-18, Tjalling C. Koopmans Research Institute (https://www.uu.nl/sites/default/files/rebo_use_dp_2010_10-18.pdf).

⁸³ Bridget Hutter & Tola Amodu, *Risk egulation and Compliance: Food Safety in the UK* (2008); on risk regulation, see generally Bridget Hutter, *Regulation and Risk: Occupational Health and Safety on the Railways* (2001).

⁸⁴ For the influential analysis of the inability of consumers to judge the quality of certain products and the consequent emergence of the “market for lemons,” see George A. Akerlof, *The Market for “Lemons”: Quality Uncertainty and the Market Mechanism*, 84 Q.J. Econ. 488 (1970).

national authorities.⁸⁵ These safeguards are particularly relevant in the sectors where the Services Directive has been implemented, which include the hospitality sector but exclude transportation services (e.g., ride-sharing platforms).⁸⁶

The traditional public interest justification of regulation has been criticized on several fronts since the 1970s. Private interest scholars contended that regulation was driven by interest groups, regulators were easily captured by the industry, and the regulatory arena was determined by a small number of regulation-seeking groups rather than by the collective welfare.⁸⁷ This “capture effect” also meant that traditional regulation was regarded as an instrument to limit competition from other providers rather than a primary tool to safeguard the quality of services and protect the public interest.⁸⁸ Despite the academic relevance of this critique, it was not supported by strong empirical evidence and provided little guidance to help detect and correct capture.⁸⁹

The criticism of public-interest regulation was also visible in the context of occupational licensing (e.g., of physicians), which was also created to regulate the quality of professions. Since the medieval guilds, multiple professions were allowed to self-regulate and decide who was allowed to join the profession and under what conditions, often collaborating closely with city councils to regulate the exchange and production of goods.⁹⁰ As described in the work of Parsons, the interests of these professions were thought to be intertwined with those of the public.⁹¹

Throughout the centuries, multiple occupation groups appeared to be driven by the wish to maintain their acquired prestige rather than by altruistic motives.⁹² This raised questions of whether self-regulation sufficed and whether regulation served the interests of the public or those of a private group.⁹³ Most traditional studies submit that licensing regulations and other authorization schemes were adopted to restrict entry and reduce competition.⁹⁴ Recent research also suggests these regulations were indeed enacted as a

⁸⁵ Maria Wiberg, *The EU Services Directive: Law or Simply Policy* 37 (2014).

⁸⁶ Vassilis Hatzopoulos & Sofia Roma, *Caring for Sharing? The Collaborative Economy under EU Law*, 54 *Common Market L. Rev.* 81 (2017).

⁸⁷ See George Stigler, *The Theory of Economic Regulation*, 2 *Bell J. Econ. & Mgmt. Sci.* 3 (1971); Richard Posner, *Theories of Economic Regulation*, 5 *Bell J. Econ. & Mgmt. Sci.* 335 (1974).

⁸⁸ On the capture theory, see Stigler, *supra* note 87. For an overview of the general challenges of the administrative state, see Richard Stewart, *Regulation, Innovation, and Administrative Law: A Conceptual Framework*, 69 *Cal. L. Rev.* 1256 (1981).

⁸⁹ Daniel Carpenter, *Detecting and Measuring Capture*, in *Preventing Regulatory Capture: Special Interest Influence and How to Limit It* 57 (Daniel Carpenter & David A. Moss eds., 2014).

⁹⁰ Peter Stabel, *Guilds in Late Medieval Flanders: Myths and Realities of Guild Life in an Export-Oriented Environment*, 30 *J. Medieval Hist.* 187, 192 (2004).

⁹¹ See Talcott Parsons, *The Social System* (1951).

⁹² See Magali Sarfatti Larson, *The Rise of Professionalism* (1977).

⁹³ Linda Haller, *Regulating the Professions*, in *The Oxford Handbook of Empirical Legal Research* 216, 217 (Peter Cane & Herbert Kritzer eds., 2010).

⁹⁴ Milton Friedman & Simon Kuznets, *Income from Independent Professional Practices* (1945).

reaction to growing risks to public safety, and to improve markets at a time when services where changing and advances in knowledge made it increasingly difficult for consumers to judge the quality of professional services.⁹⁵ One of the challenges of determining the interests underlying the need for public regulation resides in the absence of empirical evidence and the broad objections raised against regulatory capture.⁹⁶

In view of the decades of critiques aimed at the public interest arguments of regulation, several alternatives to the traditional command-and-control regulation have been suggested: the deregulation of industries; market-based approaches including pollution taxes and environmental benefit trading; self-regulation (e.g., in the financial sector); the establishment of public-private partnerships; delegation of rulemaking tasks to national and international certification bodies (e.g., sports, construction); co-regulation (e.g., media, food safety); the adoption of soft law and codes of conduct; and, more recently in some European countries, “the right to challenge.”⁹⁷

In the context of the growing intervention of private actors in regulation, we also observe the partial outsourcing of regulatory tasks to private actors justified by efficiency gains, enhanced expertise, potential for higher level of compliance, and the importance of involving different stakeholders.⁹⁸ This article regards online reputation as a separate, private enforcement mechanism that can complement traditional regulation.

B. Peer-to-Peer Regulation

The criticism of the public-interest justification of traditional regulation does not fully explain the shift to the modern system of P2P reviews. First, the legitimacy of the individuals rating and writing reviews is unclear. On the one hand, reputational mechanisms contribute to the democratic legitimacy of regulation since they enhance the broad participation of citizens in the economy;⁹⁹ they empower consumers with information and allow them to have a say. On the other hand, reputational mechanisms do not promote a true democratic pooling of expertise or a true empowerment of the

⁹⁵ Marc T. Law & Sukko Kim, Specialization and Regulation: The Rise of Professionals and the Emergence of Occupational Licensing Regulation, *J. Econ. Hist.* 723 (2005); see also Andrew T. Bond, An App for That: Local Governments and the Rise of the Sharing Economy, 90 *Notre Dame L. Rev.* 77 (2015); Vaheesan & Pasquale, *supra* note 11.

⁹⁶ Haller, *supra* note 93, at 232.

⁹⁷ See, e.g., David Driesen, Alternatives to Regulation? Market Mechanisms and the Environment, in *The Oxford Handbook of Regulation* 204 (Robert Baldwin et al. eds., 2010); Ian Ayres & John Braithwaite, *Responsive Regulation: Transcending the Deregulation Debate* (1992).

⁹⁸ See, e.g., *Government by Contract: Outsourcing and American Democracy* (Jody Freeman & Martha Minow eds., 2009); Jon Michaels, Privatization’s Pretensions, 77 *U. Chi. L. Rev.* 717 (2010); Dara O’Rourke, Outsourcing Regulation: Analyzing Nongovernmental Systems of Labor Standards and Monitoring, 31 *Pol’y Stud. J.* 1 (2003).

⁹⁹ See Sofia Ranchordás, Digital Agoras: Democratic Legitimacy, Online Participation, and the Case of Uber-Petitions, 5 *Theory & Prac. Legis.* 31 (2017).

crowd.¹⁰⁰ Many of the users who write reviews do so to promote personal agendas, to improve their own reputation, or to be eligible for a discount from a digital platform.¹⁰¹ In addition, search engines and platforms rearrange the content, streamlining what we see in practice. Some platforms assign the title of “expert” to frequent reviewers (e.g., the Yelp Elite Squad), but although they are able to offer multiple narratives of first-hand experience, it is unlikely that these individuals are more knowledgeable than regulators.¹⁰² Therefore, reputational mechanisms disrupt not only the object but also the subjects behind regulation: in the P2P economy, the regulatory instrument (i.e., the reviews) can be generated by any consumer, regardless of expertise.

Second, online reputation combines limited forms of self-regulation (e.g., conflict resolution services, basic forms for rating and processing of reviews) with the wisdom of the crowds. Therefore, it is likely that, in some cases, the regulatory effect of reputational mechanisms stems from the content of reviews rather than from the platform’s self-regulatory efforts.

Third, online rating and reputational mechanisms respond to the trust deficit that emerged in a novel situation that traditional regulation had not considered previously: the emergence of digital platforms where non-professionals could share goods with or provide services to each other. Users in the platform economy interact with individuals who are often unlicensed, unregistered non-professionals and, above all, strangers who could poison or hurt prospective consumers. Under these circumstances, users are required to trust each other and feel protected against major risks. In regulated markets, this measure of protection is typically offered by regulation that reduces mistrust in counterparties by addressing common problems such as moral hazard or high search costs.¹⁰³

Despite its informal character, online reputation provides incentives to individuals to change their behavior. However, this reputational system is far from perfect. The deficiencies of current reputational mechanisms affect their ability to protect users effectively against several risks because the information provided on P2P platforms often refers to quality features of products and services (e.g., a host’s friendliness), may be biased, and is processed in a non-transparent way. The informative and trust-building potentials of online reputation should not be disregarded, but they may not be enough to address market failures and manage important risks to consumers.

¹⁰⁰ See generally James Surowiecki, *The Wisdom of Crowds: Why the Many Are Smarter than the Few and How Collective Wisdom Shapes Business, Economies, Societies, and Nations* (2004).

¹⁰¹ Shay David & Trevor J. Pinch, *Six Degrees of Reputation: The Use and Abuse of Online Reviews and Recommendation Sites*, 11 *First Monday* (2006) (<http://firstmonday.org/ojs/index.php/fm/article/view/1315/1235>).

¹⁰² Shankhadeep Banerjee et al., *Whose Online Reviews to Trust? Understanding Reviewer Trustworthiness and Its Impact on Business*, 96 *Decision Support Sys.* 17 (2017).

¹⁰³ See Esther Keymolen, *Trust on the Line* (2016) (offering an extensive analysis of eTrust in the sharing economy).

V. A Collaborative Framework for Online Reputation

Up until now, several regulators have focused on enforcing existing rules in spite of their ability to respond to the innovative elements of the platform economy. This formal approach to regulation does not work well in the context of informal enforcement mechanisms that may also address some—but not all—risks of the platform economy.¹⁰⁴ In this Part, I suggest a co-regulatory or collaborative approach for the interaction between online reputational mechanisms and traditional regulation. Regulators can benefit from more transparent online reputational mechanisms, as they can rely on their information to identify problematic service providers that might require regulatory intervention. Online reputational mechanisms will also be more effective in managing risks if they process information in a clear and accountable way and if they are regulated.

A. Reduce Enforcement Costs

Regulatory conversations and a closer cooperation between platforms, regulators, and other stakeholders can help regulators manage risks that currently characterize the platform economy as well as reduce enforcement costs.¹⁰⁵ While official inspections of facilities take place in some sectors on a yearly basis, online reviews inspect the service and some of the facilities of restaurants, hotels, and equivalent P2P services on a daily basis. Online reputational mechanisms can alert public bodies to problems that would otherwise only be immediately identified after a formal complaint.

Rating and reputational systems complement traditional regulation by offering additional information and evidence that would otherwise be difficult to gather. In March 2017, the highest administrative court in the Netherlands criticized local enforcement officers for not considering the data included in the online reviews on Airbnb.¹⁰⁶ This public information could help public bodies ascertain whether users are in violation of local rules and proffer valid evidence to consubstantiate these infringements.

B. Co-regulation for Transparency

Reputational mechanisms rely on the observation of past actions and the ability to predict future performance on this ground. Nevertheless, observability is an imperfect method that only provides anecdotal evidence.¹⁰⁷ Online reputation results from the “noise” and the appearances created by a majority of voices. Reputational mechanisms might be untrustworthy if consumers, platforms, and regulators do not work together to overcome the limitations of this system—in particular, the scarce ratings, differing tastes,

¹⁰⁴ Robert Baldwin & Julia Black, Really Responsive Risk-Based Regulation, 32 Law & Pol’y 181 (2010).

¹⁰⁵ Julia Black, Regulatory Conversations, 29 J.L. & Soc. 163 (2002).

¹⁰⁶ Dutch Council of State, Administrative Jurisdiction Division, Mar. 15, 2017, ECLI: NL:RVS:2017:649 (<https://uitspraken.rechtspraak.nl/inziendocument?id=ECLI:NL:RVS:2017:649>) (in Dutch).

¹⁰⁷ Luis Cabral, The Economics of Trust and Reputation: A Primer 6 (2005) (<https://pdfs.semanticscholar.org/24e5/2f3bd22d4bfa86902e5ae07d57039480004f.pdf>).

and attempts to tamper with the system. The trustworthiness of online reputation as an effective regulatory mechanism depends on its ability to reduce the gap between the message conveyed by someone's reputation and the reality.

Once a user has built a sufficiently strong reputation, she might not have incentives for further investment and improvement. In addition, quality signals emitted by online reputation also fail. It is precisely when there is the risk that these signals might fail that consumers should be able to trust regulators to offer them protection, namely through the regulation of minimum standards of safety and quality.¹⁰⁸

Even when users are aware of the fact that the reviews might not be accurate or reflect any particular expertise, they take them into account because they trust that digital platforms have not been significantly altered. As Jack Balkin explains, digital platforms should be regarded as information fiduciaries and as such, they owe a duty of care and a duty of loyalty to their users.¹⁰⁹ This means that they should act competently and, in the case of online rating and reviews, ensure that the reviews are as truthful and accurate as possible.

While we cannot expect online reputational mechanisms to be infallible and always just, regulators should ensure that these systems operate in a context of procedural regularity. Platforms should be able to explain how ratings are calculated and live up to some standard of fairness and accuracy. Drawing on the scholarship of Danielle Citron and Frank Pasquale, it could be suggested that online rating and reputational mechanisms draw insights from the idea of a “technological due process”¹¹⁰—a systematic approach to deciding between automation and human discretion and ensuring that the general principles of good administration are not affected by an unaccountable delegation of regulatory tasks to informal or P2P enforcement mechanisms. Online rating and reputational mechanisms do not yet reflect the core values served by due process, those being accuracy, objectivity, the appearance of fairness, predictability, rationality, and participation.¹¹¹

Platforms can be given incentives to improve their current self-regulatory practices and their online rating and reputational mechanisms in order to guarantee that these instruments become more transparent and effective. Users write reviews following the forms they are provided with. Therefore, more accurate questions on key quality and safety aspects can significantly improve current systems. In addition, regulators should work together with platforms to address some of the negative externalities of unregulated services, namely potential socially harmful behavior. A closer cooperation between formal

¹⁰⁸ von der Crone & Vetsch, *supra* note 31, at 192.

¹⁰⁹ Jack Balkin, *Information Fiduciaries and the First Amendment*, 49 U.C. Davis L. Rev. 1185, 1207-78 (2016).

¹¹⁰ Citron & Pasquale, *supra* note 10, at 19-20; Danielle Keats Citron, *Technological Due Process*, 85 Wash. L. Rev. 1249 (2008).

¹¹¹ Kate Crawford & Jason Schultz, *Big Data and Due Process: Toward a Framework to Redress Predictive Privacy Harms*, 55 B.C. L. Rev. 93, 119 (2014).

and informal enforcement mechanisms might benefit not only public bodies but also the reliability of online reputational mechanisms.

As described in Part II, online reviews are plagued by subjective information and affected by the obscure character of platforms. Regulators and scholars have recently started to think about solutions for these problems. In May 2017, the Dutch Authority for Consumers & Markets suggested a number of improvements to the current system of online reviews, including informing consumers on how reviews are aggregated and presented; treating positive and negative reviews equally as much as possible; publishing online reviews expeditiously; ranking the most recent reviews by date of publication rather than date of writing; and providing additional information on the circumstances under which the reviews were written (e.g., “Reviewers were allowed to test this product for free” or “The reviewer received a remuneration for writing this review”).

VI. Conclusion

The high costs and failures of regulation and its public interest rationale have been well documented in the literature in recent years. Therefore, it could be tempting to suggest relying solely on self-regulatory and reputational solutions, but this article has shown that, despite their informative role, relying on these solutions might be a simplistic and incomplete approach to the imperfect information that characterizes the platform economy. Online reputation does not come at zero cost and it also requires the existence of effective sanctions.¹¹² Moreover, in the context of the platform economy, reputational feedback does not create a scenario of perfect information—it merely creates the illusion thereof. Rating and reputational systems remain black boxes which might not always produce sufficient and objective information to avoid accidents or manage other consumer risks. In the context of imperfect information, accidents might still happen, even when parties value their good name and reputation.

It is precisely here that the interaction between online reputation and regulatory intervention should be explored. As explained in the literature on product liability, the design of legal regulations should take into account the existence and effectiveness of private instruments such as market reputation.¹¹³ Traditional authorization schemes do not yet take into account the ability of consumers to provide information to each other, nor do they reckon with the general flow of information on the Internet. As information becomes a stronger regulatory instrument, traditional regulators should indeed consider reputational systems as complements to traditional state intervention.

While online reputational mechanisms might never be fully objective, a closer interaction with regulators can ensure that information provided by users is used to facilitate public enforcement, regulation is more regularly updated, different stakeholders

¹¹² Ganuza & Gomez, *supra* note 3, at 233.

¹¹³ A. Mitchell Polinsky & Steven Shavell, *The Uneasy Case for Product Liability*, 123 Harv. L. Rev. 1437, 1449, 1457 (2009).

are heard, consumers are empowered with greater transparency regarding how their reviews are processed, and the accountability deficit of reputational mechanisms is addressed.¹¹⁴ Online reputation might never be a totally objective, costless, and unbiased regulatory instrument—but, then again, neither is command-and-control regulation.

¹¹⁴ Pasquale, *supra* note 43, at 108.